INSURANCE ASSOCIATION OF CONNECTICUT

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Statement

Insurance Association of Connecticut

Insurance and Real Estate Committee

HB 6163, An Act Concerning the Territorial Classifications for Private Passenger Nonfleet Automobile Insurance Rating Plans

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I am Eric George, President of the Insurance Association of Connecticut (IAC). The Insurance Association of Connecticut opposes HB 6163, An Act Concerning the Territorial Classifications for Private Passenger Nonfleet Automobile Insurance Rating Plans.

HB 6163 would put restrictions on insurers' use of territorial rating when pricing private passenger nonfleet automobile insurance. The General Assembly has consistently rejected legislation which would eliminate or restrict the use of territorial rating. HB 6163 is no different.

Automobile insurance is sold in accordance with "cost-based pricing," which prices the insurance product according to the insurer's best estimate of how much the insured is likely to generate in claims, incorporating numerous rating factors (driving record, age of driver, age and model of car, miles driven, where the car is principally garaged, etc.) in order to develop rates equitably.

Territorial rating is an important part of cost-based pricing and is used in every state in the development of auto rates. In fact, actuarial studies have shown that territory is highly predictive of future risk, much more so than driving record. In Connecticut, territories must be approved by the

Insurance Department prior to their use. Market conduct examinations provide the Department with additional regulatory oversight concerning the use of territories.

Ratemaking data is gathered, for purposes of territorial rating, using the "principal garaging rule." For example, if a driver from Simsbury causes an accident in Hartford, the claims costs associated with that accident are charged to Simsbury, not Hartford, for purposes of ratemaking. Similarly, if that Simsbury driver's car is vandalized in Hartford, the claims costs are again charged to Simsbury. The cost of insurance reflects different degrees of risk which consumers in different territories pose. This system is used throughout the country.

What makes Connecticut unique is that, pursuant to an administrative ruling issued in 1978, the use of "pure" territorial rating is not permitted. The effects of territorial rating are reduced by a factor of 25%, as insurers are only allowed to assign 75% weight to the actual loss experience of a territory (the so-called "75/25 rule"). Due to the 75/25 rule, Connecticut drivers in territories with lower loss costs are already subsidizing the premiums paid by drivers in higher loss cost territories.

HB 6163 will greatly expand the subsidization of rates paid by drivers in high risk territories by those in lower risk territories by providing that insurers will only be allowed to assign 50% weight to the actual loss experience of a territory, further adulterating ratemaking data and preventing insurers from using cost-based pricing. There is no actuarial justification for such a change.

It is a simple, irrefutable fact, proven by decades of ratemaking data and numerous legislative and Insurance Department studies, that urban drivers are much more likely to incur auto insurance claims costs than non-urban drivers. This was again verified in 2001 by a study conducted by the National Conference of State Legislatures.

> It is a fact that policyholders from certain areas—usually higher density, more urban environs—as a group cause more at-fault accidents, and therefore, greater losses than do policyholders from other areas, as a group. (p. 61, Pricing Auto Insurance: A Study Of Ratemaking in Connecticut.)

In order to be fair, premiums must reflect that simple fact. To the contrary, HB 6163 will cause a wholesale, and unfair, shifting of costs from high risk to low risk territories. This will result in auto insurance rates increasing for most drivers in the state.

States which had previously put restrictions on the use of territory in auto insurance ratemaking have recently and emphatically repealed those restrictions. Michigan, South Carolina and New Jersey found that those restrictive laws, which were intended to help urban drivers with the cost of their insurance, actually worked to the detriment of all drivers in their state, including urban residents. By preventing insurers from being able to price their products according to the cost of the product, these states found that such laws actually created counterproductive economic effects (fewer insurers, expanded assigned risk pool, higher costs) in urban areas and across their states. In fact, Michigan repealed its territorial restrictions in 1996, in order "to facilitate the purchase of insurance at fair and reasonable prices."

The competitive marketplace is working in Connecticut to the benefit of consumers, as insurers are actively competing for business based on price, product and service. More insurers are coming into the state to engage in that market. In recent years, overall rate changes in Connecticut for auto insurance have been minimal. The assigned risk pool (the state's insurer of last resort) has continued to shrink to all-time lows (there are currently less than two hundred insureds in the pool, versus a high of about 200,000 drivers in 1988).

HB 6163, by placing artificial and counterproductive restrictions on the rating and pricing of auto insurance in this state, would cause unfair cost-shifting, impair the insurer's ability to judge risk, and do real harm to that marketplace, to the detriment of consumers across the state.

IAC urges rejection of HB 6163.